Calendar No. 958

97TH CONGRESS, 2d Session | SENATE | REPORT No. 97-667

APPLICATION OF SECTION 252 OF ECONOMIC RECOVERY TAX ACT OF 1981 TO CERTAIN TRANSFERS IN 1973

NOVEMBER 15, 1982.—Ordered to be printed

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Mr. DOLE, from the Committee on Finance, submitted the following

REPORT

[To accompany H.R. 4577]

[Including cost estimate of the Congressional Budget Office]

The Committee on Finance, to which was referred the bill (H.R. 4577) to provide that the provisions of section 252 of the Economic Recovery Tax Act of 1981 (relating to transfers of property to employees subject to certain restrictions) shall apply to certain transfers occuring during 1973 having considered the same, report favorably thereon with an amendment to the text and an amendment to the title and recommends that the bill as amended do pass.

The amendments are shown in the text of the bill in italic.

House bill.—The bill as passed by the House changes the effective date in certain cases relating to the application of section 252 of Public Law 97-34 with respect to restricted property.

Committee bill.—The bill as amended by the Committee on Finance includes the House provision, and also includes amendments with respect to (1) deferred compensation arrangements under money purchase pension plans (contained in H.R. 4948 as passed by the House), (2) effective date of withdrawal liability under the Multiemployer Pension Plan Amendments Act of 1980, (3) private foundation provisions dealing with excess business holdings, (4) application of private foundation rules to a charitable trust, and (5) application of the 10-percent excise tax on certain fishing bait.

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I. SUMMARY

Application of restricted property provision of Public Law 97-34

The bill permits certain individuals who received stock in 1973 pursuant to the exercise of employee stock options to elect to have section 252 of the Economic Recovery Tax Act of 1981 apply retroactively in certain limited circumstances. Under the bill, any reduction in tax pursuant to such election could not exceed $100,000 with respect to any one employee. The statute of limitations is amended by the bill to permit refunds or credits, or assessments, attributable to the provisions of the bill.

Salary reduction arrangements under money purchase pension plans

The Employee Retirement Income Security Act of 1974 (ERISA) provided that amounts deferred by an employee pursuant to a cash or deferred arrangement or a salary reduction arrangement under a tax-qualified profit-sharing, stock bonus or money purchase pension plan are excluded from the employee's income if (1) the plan was in existence on June 27, 1974, and (2) the applicable requirements of prior law were satisfied. This tax treatment for existing plans was preserved, pending study by the Congress of the appropriate treatment for cash or deferred and salary reduction arrangements.

Under the Revenue Act of 1978, amounts deferred by an employee after 1979 pursuant to a cash or deferred or salary reduction arrangement under a tax-qualified profit-sharing or stock bonus plan are excluded from the employee's income only if certain requirements added by the Act are met. No rules were provided by the 1978 Act for amounts deferred pursuant to similar salary reduction arrangements under a money purchase pension plan.

Under the bill, amounts deferred by an employee pursuant to a salary reduction arrangement under a money purchase pension plan will be excluded from the employee's income if the plan was in existence on June 27, 1974, and contributions by employees and the employer do not exceed the levels permitted under the plan's contribution formula on that date. In addition, with respect to years beginning after December 31, 1981, the plan is subject to rules added by the 1978 Revenue Act with respect to employee participation and prohibited discrimination in favor of officers, shareholders, or highly compensated employees. The bill will apply to money purchase pension plans maintained by taxable employers or tax-exempt organizations. The bill generally will apply for plan years beginning after 1981, and to contributions made after that date. A transition rule is provided for contributions made after 1979 and before the first plan year beginning after 1981.

Liability of employers withdrawing from multiemployer pension plans

Prior to the enactment of the Multiemployer Pension Plan Amendments Act of 1980 (MPPAA), an employer's obligation to contribute to a multiemployer pension plan generally ended when the employer withdrew from the plan, unless, within 5 years after the withdrawal, the plan terminated with insufficient assets to provide benefits at the level guaranteed by the Pension Benefit Guaranty Corporation (PBGC).

Under MPPAA, an employer who withdraws from a multiemployer pension plan generally is liable for a portion of the plan's unfunded obligations determined at the time of the withdrawal. Although the provisions of MPPAA generally became effective on September 26, 1980, the date of enactment, the withdrawal liability provisions were generally made effective retroactively to withdrawals which occurred on or after April 29, 1980.

Under the provision, withdrawal liability generally will be imposed only with respect to withdrawals occurring on or after September 26, 1980.

Private foundation rules relating to excess business holdings

The bill provides that the Otto Bremer Foundation, the El Pomar Foundation, the Houston Endowment, Inc., the Public Welfare Foundation, the Sand Springs Home, and the B. Altman Foundation may idefinitely retain certain business interests if the foundation meets certain conditions. The Ahmanson Foundation would have an additional 5 years to meet a private foundation divestiture requirement with respect to certain stock held on May 26, 1969. The New London Day Trust would not be subject to the private foundation rules applicable to charitable trusts effective for taxable years beginning after November 20, 1978.

Definition of artificial bait for purposes of the excise tax on fishing equipment

The bill excludes from the definition of "artificial bait" for purposes of the 10-percent excise tax on fishing equipment any substance which contains 85 percent (or more) by weight of plant or animal material which can be ingested by fish.

II. EXPLANATION OF THE BILL

A. Application of Restricted Property Provision of P.L. 97-34 (sec. 1 of the bill and sec. 252 of P.L. 97-34)

Present Law

In general

Under the present law rules relating to transfers of property in connection with the performance of services (Code sec. 83), an employee generally includes in income the fair market value of transferred property, less any amount paid for the property, when the property first becomes either transferable or not subject to a substantial risk of forefeiture.[1] Thus, if an employee receives property that is both subject to a substantial risk of forfeiture and is not transferable, the employee generally is not taxed until the property becomes either transferable or not subject to a substantial risk of forefeiture. The amount the employee includes in income is equal to the fair market value of the transferred property (as of the time of taxation), less any amount the employee paid for the property.

However, an employee may elect (under sec. 83(b)) to be taxed when the property is received.[2] In that case, the employee includes an amount in income equal to the fair market value of the property when received less any amount paid for the property.

Effect of restrictions

Generally, under section 83, restrictions on property are not taken into account in determining the fair market value of the property. Also, property is considered transferable for purposes of section 83 when the property would not be subject to a substantial risk of forfeiture in the hands of a subsequent transferee.

Prior to enactment of section 252 of the Economic Recovery Tax Act of 1981 (ERTA), the U.S. Tax Court had ruled [3] that stock subject to the "insider trading" rules of section 16(b) of the Securities Exchange Act of 1934 [4] as transferable within the meaning of section 83. Thus, although the taxpayer's profit on a sale of the stock within six months of receipt could be recovered by the corporation, the taxpayer was taxable on the fair market value of the stock when received.

As amended by section 252 of ERTA, section 83 provides that stock subject to the restrictions of section 16(b) of the Securities Exchange Act of 1934 is treated as being subject to a substantial risk of forfeiture and nontransferable for the six-month period following

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[1] An employer generally is allowed a business expenses deduction, when the employee is taxed, equal to the amount includible in the employee's income (sec. 83(h)).

[2] See note 1.

[3] *Horwith* v. *Comm'r*, 71 T.C. 932 (1979).

[4] 15 U.S.C. sec. 78p(b).

receipt of the stock during which that section applies. Thus, unless the taxpayer elects (under sec. 83(b)) to be taxed when the stock is received, the taxpayer must include in income (and the employer may deduct), at the expiration of the period during which section 16(b) is applicable, the value of the stock at such time, less any amount the taxpayer paid for the stock. A similar rule is provided for stock subject to restrictions on transfer by reason of complying with the "pooling-of-interests" accounting rules of Accounting Series Releases Numbered 130 ((10/5/72) 37 FR 20937; 17 CFR 211.130)) and 135 ((1/18/73) 38 FR 1734; CFR 211.135)).

The amendments made to section 83 by section 252 of ERTA apply to taxable years (of the transferee) ending after December 31, 1981.

Reasons for Change

The committee has been advised of a situation in which, prior to the effective date of ERTA section 252, stock acquired by several shareholder employees pursuant to the exercise of an option underwent a substantial diminution in value while both section 16(b) of the Securities Exchange Act of 1934 and the restrictions on transferability to comply with the "pooling-of-interests" accounting rules were in effect. The committee has concluded that in this situation, as under the rules enacted by ERTA, such shareholder employees should not be required to treat as compensation the value of the stock while subject to such limitations.

Explanation of Provision

Under the bill, the rules of section 252 of ERTA will apply if (1) stock was acquired in November or December of 1973 pursuant to options granted in November or December of 1971, (2) the corporation granting the options was acquired in a reorganization during December 1973, and (3) the fair market value of the stock in the acquiring corporation as of July 1, 1974, received in exchange for the stock acquired on exercise of the option, was less than 50 percent of its value on December 4, 1973. This relief under the bill will be allowed only at the election of a shareholder who during 1975 or 1976 sold substantially all the stock so received.

The bill will not apply with respect to a transfer to any employee to the extent that its application would result in a reduction in tax liability (exclusive of interest) of such employees in excess of $100,000 for all taxable years.

Also, the bill provides that a refund or credit of any overpayment of tax, or an assessment of any deficiency, which is attributable to provisions of the bill, and which otherwise would be barred within six months after the date of enactment, may be made or allowed to the extent attributable to application of provisions of the bill, provided that, in the case of a credit or refund, a claim therefor is filed within such six-month period.

The provisions of the bill may affect the tax liability of an electing person for the year in which stock was sold, as well as the amount of compensation and the year of its inclusion in income. The bill may also affect the amount and timing of any deduction

allowable to the employer corporation. The statute of limitations is to be kept open for the purpose of making such adjustments.

The intended beneficiaries of this bill are John G. Franzia, Jr., Joseph S. Franzia, and Fred T. Franzia.

Effective Date

The provision will have only retroactive effect, and only to the limited extent provided in the bill and described in the explanation of the provisions of the bill.

Revenue Effect

It is estimated that this provision will reduce budget receipts by a negligible amount.

B. Salary Reduction Arrangements Under Money Purchase Pension Plans (sec. 2 of the bill and secs. 401(k) and 402(a) of the Code)

Present Law

In general

A money purchase pension plan is a defined contribution plan under which each participant's pension benefit is based solely on the balance of the participant's account, consisting of contributions, income, gain, expenses, and losses. Profit-sharing plans are also defined contribution plans.

Under a profit-sharing plan with a cash or deferred arrangement, or under a money purchase pension plan with a salary reduction arrangement, the employer gives an employee the choice of (1) receiving a specified amount in cash as current compensation or (2) having that amount contributed by the employer to the plan.

In December 1972, the Internal Revenue Service issued proposed regulations which called into question the tax treatment of amounts contributed to qualified plans pursuant to such salary reduction arrangements. (These proposed regulations were withdrawn in July 1978). Under the rules in effect at the time of the proposal, an employee generally was not taxed currently on amounts the employee chose to have contributed pursuant to a salary reduction arrangement. Under the proposed regulations, amounts contributed to a plan by the employer due to the election of the employee would be included in the employee's income.

Freeze on tax treatment

In order to allow time for Congressional study of this area, ERISA provided that the tax treatment of employer contributions under cash or deferred or other salary reduction arrangements in existence on June 27, 1974, was to be governed under the law as it was applied prior to January 1, 1972. Accordingly, the employer contributions were not includible in the income of covered employees, provided the plans satisfied the requirements of pre-1972 law and otherwise complied with the tax-qualification rules. Under ERISA, this freeze in tax treatment was continued through 1976, or (if later) until regulations were issued in final form which would change the pre-1972 administration of the law. The freeze was subsequently extended through 1979.

Revenue Act of 1978

The Revenue Act of 1978 provided rules for new and old profit-sharing plans with cash or deferred arrangements. The new rules, which also apply to stock bonus plans, are effective for plan years beginning after 1979. For years beginning before 1980, the tax

treatment under a plan in existence on June 27, 1974, is determined under prior law. No new rules were provided by the 1978 act for salary reduction arrangements under money purchase pension plans.

Reason for Change

Many tax-exempt organizations have money purchase pension plans with a salary reduction feature. Because these organizations are generally precluded from adopting profit-sharing plans or stock bonus plans, the committee believes that employers who have previously established such plans should be able to continue to maintain them.

Explanation of Provision

The provision revises the tax-qualification rules to permit a qualified money purchase pension plan which was in existence on June 27, 1974, and which provided for a salary reduction arrangement on that date, to continue the arrangement after 1979. However, this revision to the tax-qualification rules will apply only to those money purchase pension plans under which employer and employee contributions may not exceed the limits (e.g., the percentage of pay) provided under the plan's contribution formula on June 27, 1974.

In addition, for plan years beginning after December 31, 1981, a salary reduction arrangement under a money purchase pension plan is subject to the special tax-qualification rules for cash or deferred arrangements added by the 1978 Revenue Act with respect to employee eligibility to participate in the arrangement and to prohibited discrimination in favor of highly compensated employees. These rules presently apply to cash or deferred arrangements under qualified profit-sharing or stock bonus plans.

The provision applies to salary reduction arrangements under money purchase pension plans of taxable employers and tax-exempt organizations.

Effective Date

The provision generally will apply for plan years beginning after December 31, 1981, and to contributions made after that date. A transition rule is provided for plan years and contributions made after 1979, and before the beginning of the first plan year beginning after 1981.

Revenue Effect

It is estimated that the provision will have a negligible effect on budget receipts.

C. Liability of Employers Withdrawing From Multiemployer Pension Plans (sec. 3 of the bill, secs. 4211, 4217, 4219, 4235, and 4402 of ERISA, and sec. 108 of the Multiemployer Pension Plan Amendments Act of 1980)

Present Law

The liability of an employer who withdraws from a multiemployer pension plan for a portion of the plan's unfunded pension obligations is determined pursuant to title IV of the Employee Retirement Income Security Act of 1974 (ERISA). Under ERISA, prior to its amendment by the Multiemployer Pension Plan Amendments Act of 1980 (MPPAA), an employer's liability generally ended when the employer withdrew from the plan unless, within 5 years after the withdrawal, the plan terminated with insufficient assets to provide benefits at the level guaranteed by the Pension Benefit Guaranty Corporation (PBGC). In the event of such a termination, each employer who maintained the plan during the 5-year period preceding the termination was potentially liable to the PBGC for a share of the insufficiency. An employer's liability generally was limited, however, to 30 percent of its net worth.

MPPAA amended ERISA to provide that an employer who totally or partially withdraws from a multiemployer pension plan generally is liable for a portion of the plan's unfunded obligations determined at the time of the withdrawal (computed under one of several alternative specified methods). Employers in the building and construction or entertainment industries are relieved of withdrawal liability if certain requirements are met. A de minimis exception is provided for relatively small liabilities.

Although the provisions of MPPAA generally became effective on September 26, 1980, the date of enactment, the withdrawal liability provisions generally were made effective for withdrawals which occurred after April 28, 1980 (the date of a Senate Finance Committee markup on a bill extending prior law).

Reasons for Change

The committee concluded that it was generally inappropriate to impose withdrawal liability under the provisions of MPPAA with respect to withdrawals occurring prior to the enactment of the Act.

Explanation of Provision

Under the provision, withdrawal liability generally will be imposed under the provisions added by MPPAA only with respect to an employer's withdrawal from a multiemployer plan occurring after September 25, 1980. Liability for withdrawals occurring before September 26, 1980, will be determined pursuant to the 5-year rule originally provided by ERISA. Thus, for an employer

who withdraws before September 26, 1980, liability generally will be imposed only if the plan terminates before the earlier of September 26, 1985, or the expiration of 5 years after the date of the withdrawal, with insufficient assets.

In addition, under the provision, (1) any liability previously imposed under MPPAA with respect to withdrawals occurring after April 28, 1980, but before September 26, 1980, will generally be voided, and (2) any amounts paid by an employer to a plan sponsor as a result of the imposition of such liability under MPPAA with respect to a withdrawal occurring prior to September 26, 1980, would be refunded (net of reasonable administrative expenses). The provision does not increase an employer's liability under MPPAA except to the extent that liability may be affected by an increase in unfunded obligations for vested benefits under a plan because the withdrawal liability of another employer is voided.

Effective Date

The provision effective upon enactment.

Revenue Effect

It is estimated that the provision will have a negligible impact on revenues.

D. Private Foundation Rules Relating to Excess Business Holdings

Present Law

The Tax Reform Act of 1969 imposed an excise tax on the excess business holdings of a private foundation (Code sec. 4943). Generally under the excess business holdings provisions, the combined ownership of a business by private foundation and all disqualified persons cannot exceed 20 percent of the voting stock of the business (35 percent if other persons have effective control of the business).

The 1969 Act provided that, if a private foundation and disqualified persons together had holdings on May 26, 1969, in excess of the permitted amounts under the general rules, then those holdings could be retained for a transitional period during which the combined holdings have to be reduced to 50 percent (ultimately to 35 percent if the disqualified persons hold, in the aggregate, no more than 2 percent of the business; if they hold more than 2 percent, then the combined holdings may continue to be as much as 50 percent, of which the foundation itself may hold not more than 25 percent).

a. Exemption from divestiture requirements of excess business holdings provision for the El Pomar Foundation (sec. 4(a) of the bill and sec. 101 (*l*)(4)(D)(i) of the Tax Reform Act of 1969)

Reasons for Change

The committee believes that it is appropriate to provide an exemption from the divestiture requirements of the excess business holdings provision of present law with respect to ownership of the Broadmoor Hotel by the El Pomar Foundation of Colorado Springs, Colorado.

Explanation of Provision

Under the bill, the El Pomar Foundation of Colorado Springs, Colorado will not be required to divest itself of the interests which it held on May 26, 1969, (directly or indirectly) in the Broadmoor Hotel in order to avoid the excise taxes under section 4943 on excess business holdings. This exemption from the section 4943 divestiture requirements does not apply to any interests which may be held by the El Pomar Foundation in any business enterprise other than its direct or indirect holdings in the Broadmoor Hotel.

Effective Date

The provision is effective on the date of enactment.

Revenue Effect

It is estimated that this provision will have no effect on budget receipts through fiscal year 1987.

b. Exemption from divestiture requirements of excess business holdings provision for the Houston Endowment, Inc. and the Public Welfare Foundation (sec. 4(a) of the bill and sec. 101(*l*)(4)(D)(ii) and (iii) of the Tax Reform Act of 1969)

Reasons for Change

The committee believes that it is appropriate to provide an exemption from the divestiture requirements of the excess business holdings provision of present law with respect to ownership of the Houston Chronicle Publishing Company by the Houston Endowment, Inc., of Houston, Texas and Spartanberg Herald and Journal, the Gadsden Times, or the Tuscaloosa News by the Public Welfare Foundation of Washington, D.C. However, in the case of the Houston Endowment, Inc., the committee was concerned that the Houston Chronicle Publishing Company not obtain a competitive advantage over other newspapers through its ownership by the Houston Endowment, Inc.

Explanation of Provision

Under the bill, the Houston Endowment, Inc. of Houston, Texas, and the Public Welfare Foundation of Washington, D.C. will not be required to divest themselves of the interests which they held on May 26, 1969, in the Houston Chronicle Publishing Company or in the Spartanberg Herald and Journal, the Gadsden Times, or the Tuscaloosa News in order to avoid the excise taxes under section 4943 on excess business holdings. This exemption from the section 4943 divestiture requirements does not apply to interests held by those foundations in any other business enterprise other than their direct or indirect holdings in those newspapers. In the case of the Houston Endowment, Inc., the exemption from the divestiture rules only applies so long as the Houston Chronicle Publishing Company is generally operated in accordance with the standards of efficiency and profitability prevailing in the newspaper industry in the United States from time to time.

Effective Date

The provision is effective on the date of enactment.

Revenue Effect

It is estimated that this provision will have no effect on budget receipts through fiscal year 1987.

c. Exemption from divestiture requirements of excess business holdings provision for the Sand Springs Home (sec. 4(a) of the bill and sec. 101(*l*)(4)(D)(iv) of the Tax Reform Act of 1969)

Reasons for Change

The committee believes that it is appropriate to provide an exemption from the divestiture requirements of the excess business holdings provision of present law with respect to ownership of certain businesses by the Sand Springs Home of Sand Springs, Oklahoma.

Explanation of Provision

Under the bill, the Sand Springs Home of Sand Springs, Oklahoma will not be required to divest itself of the interests which it held on May 26, 1969, (directly or indirectly) in certain businesses in order to avoid the excise taxes under section 4943 on excess business holdings. This exemption from the section 4943 divestiture requirements does not apply to any interests which may be held by the Sand Springs Home in any business enterprise other than its direct or indirect holdings in those businesses.

Effective Date

The provision is effective on the date of enactment.

Revenue Effect

It is estimated that this provision will have no effect on budget receipts through fiscal year 1987.

d. Exemption from divestiture requirements of excess business holdings provision for the Otto Bremer Foundation (sec. 4(a) of the bill and sec. 101(*l*)(4)(D)(v) of the Tax Reform Act of 1969)

Reasons for Change

The committee believes that it is appropriate to provide an exemption from the divestiture requirements of the excess business holdings provision of present law with respect to the ownership of certain banks and bank-related companies by the Otto Bremer Foundation of St. Paul, Minnesota.

Explanation of Provision

Under the bill, the Otto Bremer Foundation of St. Paul, Minnesota will not be required to divest itself of the interests which it held on May 26, 1969, (directly or indirectly) in a bank holding company or of any stock owned, directly or indirectly, by such bank holding company on September 28, 1982 and bank-related companies in order to avoid the excise taxes under section 4943 on excess business holdings. This exemption from the section 4943 divestiture requirements does not apply to any interests which may be held by the Otto Bremer Foundation in any business enterprise other than its direct or indirect holdings in those companies.

Effective Date

The provision is effective on the date of enactment.

Revenue Effect

It is estimated that this provision will have no effect on budget receipts through fiscal year 1987.

e. Exemption from divestiture requirements of excess business holdings provision for the Altman Foundation (sec. 4(a) of the bill and sec. 101(*l*)(4)(D)(vi) of the Tax Reform Act of 1969)

Reasons for Change

The committee believes that it is appropriate to provide an exemption from the divestiture requirements of the excess business holdings provision of present law with respect to ownership of B. Altman & Co. by the Altman Foundation of New York, New York.

Explanation of Provision

Under the bill, the Altman Foundation of New York, New York will not be required to divest itself of the interests which it held on May 26, 1969, (directly or indirectly) in B. Altman & Co. in order to avoid the excise taxes under section 4943 on excess business holdings. This exemption from the section 4943 divestiture requirements does not apply to any interests which may be held by the Altman Foundation in any business enterprise other than its direct or indirect holdings in B. Altman & Co.

Effective Date

The provision is effective on the date of enactment.

Revenue Effect

It is estimated that this provision will have no effect on budget receipts through fiscal year 1987.

f. Extension of time to meet the divestiture requirements of the excess business holdings provision for the Ahmanson Foundation (sec. 4(a) of the bill and sec. 101(*l*)(4)(E) of the Tax Reform Act of 1969)

Reasons for Change

Because of litigation with the State of California which lasted until 1978, the Ahmanson Foundation has not had as long a period to dispose of its excess business holdings as other foundations. Accordingly, the committee believes that the Ahmanson Foundation should be granted an additional 5-year period to dispose of its excess business holdings.

Explanation of Provision

The bill allows an additional 5-year period (until May 26, 1989) for the Ahmanson Foundation of Los Angeles, California, to divest itself of its excess business holdings in the H.F. Ahmanson & Co.

Effective Date

The provision is effective on the date of enactment.

Revenue Effect

It is estimated that this provision will have no effect on budget receipts through fiscal year 1987.

E. Exclusion of the New London Day Trust From the Rules Appl cable to Private Foundations (sec. 4(b) of the bill and sec 4947(a)(1) of the Code)

Present Law

The Tax Reform Act of 1969 imposed a series of regulatory excise taxes on private foundations and imposed a tax on their investment income (Code secs. 4940–4946). In addition, the 1969 Act treated certain wholly charitable trusts as private foundations and generally subjected those trusts to the same rules applicable to private foundations (sec. 4947(a)(1)).

Reasons for Change

The committee believes that the operations of the New London Day Trust, including its operation of the New London Times, should not be subject to the regulatory taxes or the tax on investment income applicable to private foundations.

Explanation of Provision

The bill provides that the New London Day Trust, which is a trust with exclusively charitable interests and substantially all of whose assets consist of the stock in the New London Times, is not to be treated as a private foundation under section 4947(a)(1).

Effective Date

The provision applies to taxable years beginning after November 20, 1978.

Revenue Effect

It is estimated that this provision will have a negligible revenue effect.

F. Definition of Artificial Bait for Purposes of the Excise Tax on Fishing Equipment (sec. 5 of the bill and sec. 4161(a) of the Code)

Present Law

Under present law, a 10-percent excise tax is imposed upon the sales price of fishing rods, creels, and reels, and on artificial lures, baits, and flies (including parts or accessories of such articles sold on or in connection therewith, or with the sale thereof) by the manufacturer, producer, or importer (sec. 4161(a)).

There is no statutory definition of "artificial bait" to which the tax applies. However, Treasury Regulations (Treas. Reg. § 48.4161(a)-2(d)) define the term "artificial lures, baits, and flies" to include all artifacts, of whatever materials made, that simulate an article considered edible by fish, and that are designed to be attached to a line or hook to attract fish so that they may be captured. Thus, the term includes such artifacts as imitation flies, blades, spoons, spinners, etc., and edible materials that have been processed so as to resemble a different edible article considered more attractive to fish, such as bread crumbs treated so as to simulate salmon eggs, and pork rind cut and dyed to resemble frogs, eels, or tadpoles.

The Internal Revenue Service has taken the position that bait which contains very little artificial substance may be subject to the excise tax. In Revenue Ruling 71-321, 1971-2 C.B. 369, the Service held that edible food items which are shaped or treated to give the appearance or odor of insects, flies, worms, frogs, etc., are artifical lures or baits. In addition, in Revenue Ruling 77-302, 1977-2 C.B. 374, the Service held that a floating fish bait that is manufactured from a semi-soft cheese food to which ingredients are added to provide the desired consistency, color, scent, and buoyancy and which is then packaged by weight and sold in a solid form that the user may shape or form, as with a fish hook, is an artificial bait or lure subject to the manufacturer's excise tax.

Reasons for Change

The excise tax on fishing equipment applies to artificial bait, but is not intended to apply to bait consisting of natural substances. The committee does not believe that the addition of small amounts of artificial matter to an otherwise edible product is a sufficient alteration to change the basic character of the product. Therefore, the committee has determined that bait comprised of at least 85 percent edible substances should not be subject to the excise tax on "artificial" bait.

Explanation of Provision

This bill excludes from the definition of "artificial bait" any substance which contains 85 percent or more by weight of plant or animal material which can be ingested by fish. Thus, those types of substances are exempt from the 10-percent excise tax on fishing equipment.

The committee does not necessarily intend, however, that this provision result in all substances used as bait and containing less than 15 percent edible material being classified as "artificial" bait. Rather, the 85-percent rule is intended to be a "safe-harbor." If a fish bait product is comprised of less than 85 percent by weight of plant or animal material which can be ingested by fish, the determination of whether the bait is "artificial bait" must be made on a case-by-case basis in light of the pertinent facts involved.

Although this provision may benefit other taxpayers, it is intended primarily to benefit the Don Rich Company, Inc., of La Canada, California, which produces "Zeke's Floatin' Bait." This bait has a base of processed cheese to which is added certain artificial ingredients which make the cheese easier to thin and mix and which give the bait its flotation characteristics.

Effective Date

The provision applies with respect to sales made after December 31, 1979.

Revenue Effect

It is estimated that this provision will reduce budget receipts by a negligible amount.

III. COSTS OF CARRYING OUT THE BILL AND VOTE OF THE COMMITTEE IN REPORTING H.R. 4577

Budget Effects

In compliance with paragraph 11(a) of Rule XXVI of the Standing Rules of the Senate, the following statement is made relative to the budget effects of H.R. 4577, as reported.

Budget receipts

The committee estimates that the provisions in this bill will reduce budget receipts by less than $1 million annually during fiscal years 1983 through 1987.

The Treasury Department agrees with this statement.

Budget outlays

The bill involves no budget outlays.

Vote of the Committee

In compliance with paragraph 7(c) of Rule XXVI of the Standing Rules of the Senate, the following statement is made relative to the vote by the committee on the motion to report the bill. H.R. 4577, as amended, was ordered favorably reported by voice vote.

IV. REGULATORY IMPACT OF THE BILL AND OTHER MATTERS TO BE DISCUSSED UNDER SENATE RULES

A. Regulatory Impact

Pursuant to paragraph 11(b) of Rule XXVI of the Standing Rules of the Senate, the committee makes the following statement concerning the regulatory impact that might be incurred in carrying out the provisions of H.R. 4577, as reported.

Numbers of individuals and businesses who would be regulated

The bill does not involve new or expanded regulation of individuals or businesses.

Economic impact of regulation on individuals, consumers, and businesses

The bill makes changes with respect to the effective date of the restricted property provision of P.L. 97-34, deferred compensation arrangements under money purchase pension plans, effective date of withdrawal liability for multiemployer pension plans, private foundation rules relating to excess business holdings, private foundation rules relating to charitable trusts, and the definition of artificial bait for purposes of the excise tax on fishing equipment.

Impact on personal privacy

The bill does not relate to the personal privacy of individuals.

Determination of the amount of paperwork

The bill will involve little, if any, additional paperwork for taxpayers.

B. Other Matters

Consultation with Congressional Budget Office on budget estimates

In accordance with section 403 of the Budget Act, the committee advises that the Director of the Congressional Budget Office has examined the committee's budget estimates of the tax provisions of the bill (as shown in Section III of this report) and agrees with the methodology used and the committee's budget estimates. The Director submitted the following statement:

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE,
Washington, D.C., October 18, 1982.

Hon. ROBERT DOLE,
Chairman, Committee on Finance, U.S. Senate, Washington, D.C.

DEAR MR. CHAIRMAN: In accordance with the Budget Act, the Congressional Budget Office has examined H.R. 4577, as amended by the Committee on Finance. The original bill as passed by the

House of Representatives permits certain individuals who received stock in 1973 pursuant to the exercise of employee stock options to elect to have Section 252 of the Economic Recovery Tax Act of 1981 apply retroactively. The Committee on Finance approved the bill with four amendments dealing with money purchase pension plans, multi-employer pension plans, private foundation excess business holding rules, and an excise tax on fishing bait.

This bill does not provide any new budget authority. The provision dealing with money purchase pension plans increases an existing tax expenditure.

In accordance with Section 403 of the Budget Act, the Congressional Budget Office has reviewed the revenue estimates provided by the staff of the Joint Committee on Taxation, and agrees with the methodology used and the resulting estimates. It is estimated that this bill will reduce budget receipts by less than $1 million per fiscal year beginning in 1983.

The individual revenue estimates of the five provisions of the bill are outlined in the attached table.

Sincerely,

ALICE M. RIVLIN, *Director.*

ESTIMATED REVENUE EFFECTS OF H.R. 4577, APPLICATION OF SECTION 252 OF THE ECONOMIC RECOVERY TAX ACT OF 1981 TO CERTAIN TRANSFERS IN 1973

[Fiscal years, in millions of dollars]

	1983	1984	1985	1986	1987
Restricted property	a	a	a	a	a
Money purchase pension plans*	a	a	a	a	a
Multi-employer pension plans	a	a	a	a	a
Private foundations	a	a	a	a	a
Excise tax on fishing bait	*a*	*a*	*a*	*a*	*a*
Total	b	b	b	b	b

a. Negligible.
b. Less than $1 million.
* Tax expenditure.

New budget authority

In compliance with section 308(a)(1) of the Budget Act, and after consultation with the Director of the Congressional Budget Office, the committee states that the changes made to existing law by the bill involves no new budget authority.

Tax expenditures

In compliance with section 308(a)(2) of the Budget Act with respect to tax expenditures, and after consultation with the Director of the Congressional Budget Office, the committee states that the changes made to existing law by section 2 of the bill (money purchase pension plans) involve a negligible increase in tax expenditures.

V. CHANGES IN EXISTING LAW MADE BY THE BILL, AS REPORTED

In the opinion of the committee, it is necessary, in order to expedite the business of the Senate, to dispense with the requirements of paragraph 12 of Rule XXVI of the Standing Rules of the Senate (relating to the showing of changes in existing law made by the provisions of H.R. 4577, as reported by the committee).